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2005 OCT 26 A 8:50

MEMORANDUM

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AZ CORP COMMISSION  
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TO: THE COMMISSION

FROM: Utilities Division

DATE: October 26, 2005

RE: IN THE MATTER OF THE PURCHASED GAS ADJUSTOR BANK BALANCE  
THRESHOLD LEVEL FOR UNS GAS, INC. (DOCKET NO. G-04204A-05-0046)

In Decision No. 67730 (March 31, 2005), the Commission approved a \$0.03 per therm purchased gas adjustor ("PGA") surcharge for UNS Gas, Inc. ("UNS"). In that Order, the Commission also ordered that "Staff and the Company shall come up with a new threshold amount for the bank balance. This recommendation shall be submitted to the Commission by December 31, 2005."

Through the summer and fall of 2005, Staff and UNS have held a number of discussions regarding the PGA bank balance threshold (aka trigger). The end result of these discussions is that Staff and UNS have identified similar levels at which they would like to see the bank balance threshold reset to. However, UNS has indicated to Staff that there are additional issues beyond the bank balance threshold that the Company wishes to raise in the context of this proceeding. In Staff's view, Decision No. 67730 only directed the parties to address the bank balance threshold issue and therefore Staff did not feel it would be appropriate to address any issues beyond the threshold issue in this proceeding. Therefore, Staff and UNS agreed that Staff and UNS would present their recommendations separately so that UNS could have the opportunity to identify and discuss the additional issues they would like the Commission to consider. It is Staff's understanding that approximately concurrent with the filing of Staff's Memo in this proceeding, UNS will separately make a filing containing its recommendations and attendant discussions.

Regarding the level of the bank balance threshold, \$4,450,000 for UNS currently, the bank balance threshold level was set as part of the proceeding in 1998 when the Commission moved to the banded 12-month rolling average PGA mechanism. For each Arizona local distribution company ("LDC"), the company's sales for 1996 and 1997 were averaged and then multiplied by \$0.05 per therm to create the PGA bank balance threshold for each LDC. At the time, it was recognized that by nature the setting of such a threshold level was rather arbitrary, and it was also recognized that if an LDC's sales changed significantly the level of the threshold might need to be revisited. The general intent in setting a threshold level for each LDC was that the threshold would trigger some type of action by the company to come to the Commission to address the bank balance when it reached or exceeded the designated level, precluding the possibility of enormous growth in the bank balance without consideration of any substantive action to address it. Since the time when the threshold levels were set in 1998, UNS, as

successor to Citizens' gas properties in Arizona, has seen significant growth in consumption, and natural gas market conditions have also changed dramatically.

The average annual sales for Citizens' Arizona Gas Divisions in 1996 and 1997 was approximately 88.7 million therms. Multiplying this number by \$0.05 per therm and rounding off resulted in a trigger level of \$4,450,000. It should be noted that at the time Citizens had two operating divisions, Northern Arizona and Santa Cruz, and that these divisions were merged as part of the proceeding where UNS acquired Citizens' Arizona natural gas assets. The average annual sales for UNS in 2003 and 2004 increased to approximately 106.9 million therms, a 20.55 percent increase over the 1996/1997 level. Applying the same \$0.05 per therm methodology to the updated sales level would result in a possible new rounded off threshold level of \$5,345,000, an increase of \$895,000 over the current threshold.

Beyond this basic adjustment for higher annual sales, there is the question of whether any further adjustment should be made to the threshold level for other reasons, such as high and more volatile natural gas prices. For example, if there were a desire to adjust the threshold level to fully reflect the growth in total annual gas cost for UNS, the threshold would then be increased to \$12,690,000, reflecting the 185.16 percent increase on average annual gas costs from 1996/1997 to 2003/2004, from approximately \$21.5 million to \$61.5 million. An adjustment corresponding directly to the growth in the cost of gas would represent a very large increase in the threshold level and would likely cause concern on the part of UNS.

Another option would be to increase the threshold level to capture growth in the volume of therm sales discussed above, plus provide some level of recognition for higher and more volatile natural gas prices. One possible way to do this would be to double the \$895,000 threshold increase resulting from higher usage, resulting in a threshold of \$6,240,000. This potential threshold level, while approaching a 50 percent increase, is not so large that it would represent an enormous new exposure to ratepayers or the company, but would provide some level of additional flexibility for the bank balance to move within the threshold level, and Staff believes that such a proposed threshold level is reasonable.

It is worth noting that the adjustment to UNS' threshold being proposed herein by Staff employs the same methodology as was employed in Staff's recommendation in the on-going Southwest Gas rate proceeding (Docket No. G-01551A-04-0876).

To date, the bank balance threshold has been applied symmetrically, with the same level being applied to both under and over-collected PGA bank balances. One option the Commission may wish to consider would be to revise the threshold in a manner which creates asymmetrical threshold levels for under and over-collected bank balances. For example, the Commission could choose to increase the threshold level applicable to under-collected bank balances, but keep the threshold level at the current level for over-collected bank balances.

THE COMMISSION

October 26, 2005

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An important point in considering the threshold level is that reaching that given level does not necessarily result in any PGA surcharge being implemented or any specific action being taken by the Commission. The threshold simply serves as a symbolic waypoint to highlight that the bank balance is becoming relatively large, that the Company should come to the Commission in some manner to address it, and that the Commission may choose to act on it in some fashion. Any change in the threshold level needs to carefully balance a variety of issues including sales levels, natural gas market conditions, interest accumulations on any under or over-collected bank balance, the likelihood of the Company filing more or less often to address bank balance levels, the general interest in having the cost causer pay for gas costs, and impacts on the Company and customers of carrying bank balances of varying sizes and durations.

Taking these issues into consideration, Staff recommends that UNS' threshold level on the PGA bank balance be increased to \$6,240,000.

A handwritten signature in black ink, appearing to read 'EGJ', with a long horizontal line extending to the right.

Ernest G. Johnson  
Director  
Utilities Division

EGJ:RGG:lm\VG

ORIGINATOR: Robert Gray

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**BEFORE THE ARIZONA CORPORATION COMMISSION**

JEFF HATCH-MILLER  
Chairman  
WILLIAM A. MUNDELL  
Commissioner  
MARC SPITZER  
Commissioner  
MIKE GLEASON  
Commissioner  
KRISTIN K. MAYES  
Commissioner

IN THE MATTER OF PURCHASED GAS  
ADJUSTOR THRESHOLD LEVEL FOR  
UNS GAS, INC.

DOCKET NO. G-04204A-05-0046  
DECISION NO. \_\_\_\_\_  
ORDER

Open Meeting  
November 8 and 9, 2005  
Phoenix, Arizona

BY THE COMMISSION:

FINDINGS OF FACT

1. UNS Gas, Inc. ("UNS") is engaged in providing natural gas service within portions of Arizona, pursuant to authority granted by the Arizona Corporation Commission.
  2. In Decision No. 67730 (March 31, 2005), the Commission approved a \$0.03 per therm purchased gas adjustor ("PGA") surcharge for UNS. In that Order, the Commission also ordered that "Staff and the Company shall come up with a new threshold amount for the bank balance. This recommendation shall be submitted to the Commission by December 31, 2005."
  3. Through the summer and fall of 2005, Staff and UNS have held a number of discussions regarding the PGA bank balance threshold (aka trigger).
  4. The end result of these discussions is that Staff and UNS have identified similar levels at which they would like to see the bank balance threshold reset to. However, UNS has indicated to Staff that there are additional issues beyond the bank balance threshold that the Company wishes to raise in the context of this proceeding.
- ...

1           5.       In Staff's view, Decision No. 67730 only directed the parties to address the bank  
2 balance threshold issue and therefore Staff did not feel it would be appropriate to address any  
3 issues beyond the threshold issue in this proceeding. Therefore, Staff and UNS agreed that Staff  
4 and UNS would present their recommendations separately so that UNS could have the opportunity  
5 to identify and discuss the additional issues they would like the Commission to consider.

6           6.       It is Staff's understanding that approximately concurrent with the filing of Staff's  
7 Memo in this proceeding, UNS will separately make a filing containing its recommendations and  
8 attendant discussions.

9           7.       Regarding the level of the bank balance threshold, \$4,450,000 for UNS currently,  
10 the bank balance threshold level was set as part of the proceeding in 1998 when the Commission  
11 moved to the banded 12-month rolling average PGA mechanism. For each Arizona local  
12 distribution company ("LDC"), the company's sales for 1996 and 1997 were averaged and then  
13 multiplied by \$0.05 per therm to create the PGA bank balance threshold for each LDC.

14          8.       At the time, it was recognized that by nature the setting of such a threshold level  
15 was rather arbitrary, and it was also recognized that if an LDC's sales changed significantly the  
16 level of the threshold might need to be revisited. The general intent in setting a threshold level for  
17 each LDC was that the threshold would trigger some type of action by the company to come to the  
18 Commission to address the bank balance when it reached or exceeded the designated level,  
19 precluding the possibility of enormous growth in the bank balance without consideration of any  
20 substantive action to address it.

21          9.       Since the time when the threshold levels were set in 1998, UNS, as successor to  
22 Citizens' gas properties in Arizona, has seen significant growth in consumption, and natural gas  
23 market conditions have also changed dramatically.

24          10.       The average annual sales for Citizens' Arizona Gas Divisions in 1996 and 1997 was  
25 approximately 88.7 million therms. Multiplying this number by \$0.05 per therm and rounding off  
26 resulted in a trigger level of \$4,450,000.

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11. It should be noted that at the time Citizens had two operating divisions, Northern Arizona and Santa Cruz, and that these divisions were merged as part of the proceeding where UNS acquired Citizens' Arizona natural gas assets.

12. The average annual sales for UNS in 2003 and 2004 increased to approximately 106.9 million therms, a 20.55 percent increase over the 1996/1997 level. Applying the same \$0.05 per therm methodology to the updated sales level would result in a possible new rounded off threshold level of \$5,345,000, an increase of \$895,000 over the current threshold.

13. Beyond this basic adjustment for higher annual sales, there is the question of whether any further adjustment should be made to the threshold level for other reasons, such as high and more volatile natural gas prices.

14. For example, if there were a desire to adjust the threshold level to fully reflect the growth in total annual gas cost for UNS, the threshold would then be increased to \$12,690,000, reflecting the 185.16 percent increase on average annual gas costs from 1996/1997 to 2003/2004, from approximately \$21.5 million to \$61.5 million.

15. An adjustment corresponding directly to the growth in the cost of gas would represent a very large increase in the threshold level and would likely cause concern on the part of UNS.

16. Another option would be to increase the threshold level to capture growth in the volume of therm sales discussed above, plus provide some level of recognition for higher and more volatile natural gas prices.

17. One possible way to do this would be to double the \$895,000 threshold increase resulting from higher usage, resulting in a threshold of \$6,240,000. This potential threshold level, while approaching a 50 percent increase, is not so large that it would represent an enormous new exposure to ratepayers or the company, but would provide some level of additional flexibility for the bank balance to move within the threshold level, and Staff believes that such a proposed threshold level is reasonable.

...

...

18. It is worth noting that the adjustment to UNS' threshold being proposed herein by Staff employs the same methodology as was employed in Staff's recommendation in the on-going Southwest Gas rate proceeding (Docket No. G-01551A-04-0876).

19. To date, the bank balance threshold has been applied symmetrically, with the same level being applied to both under and over-collected PGA bank balances. One option the Commission may wish to consider would be to revise the threshold in a manner which creates asymmetrical threshold levels for under and over-collected bank balances. For example, the Commission could choose to increase the threshold level applicable to under-collected bank balances, but keep the threshold level at the current level for over-collected bank balances.

20. An important point in considering the threshold level is that reaching that given level does not necessarily result in any PGA surcharge being implemented or any specific action being taken by the Commission. The threshold simply serves as a symbolic waypoint to highlight that the bank balance is becoming relatively large, that the Company should come to the Commission in some manner to address it, and that the Commission may choose to act on it in some fashion.

21. Any change in the threshold level needs to carefully balance a variety of issues including sales levels, natural gas market conditions, interest accumulations on any under or over-collected bank balance, the likelihood of the Company filing more or less often to address bank balance levels, the general interest in having the cost causer pay for gas costs, and impacts on the Company and customers of carrying bank balances of varying sizes and durations.

22. Staff, having taken these issues into consideration, recommended that UNS' threshold level on the PGA bank balance be increased to \$6,240,000.

#### CONCLUSIONS OF LAW

1. UNS is an Arizona public service corporation within the meaning of Article XV, Section 2, of the Arizona Constitution.

2. The Commission has jurisdiction over UNS and over the subject matter of the application.

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3. The Commission, having reviewed the application and Staff's Memorandum dated October 26, 2005, concludes that it is in the public interest to approve an increase in the PGA bank balance threshold level to \$6,240,000.

ORDER

IT IS THEREFORE ORDERED that the proposed increase in the PGA bank balance threshold level to \$6,240,000 is approved.

IT IS FURTHER ORDERED that this Order shall become effective immediately.

**BY THE ORDER OF THE ARIZONA CORPORATION COMMISSION**

CHAIRMAN

COMMISSIONER

COMMISSIONER

COMMISSIONER

COMMISSIONER

IN WITNESS WHEREOF, I BRIAN C. McNEIL, Executive Director of the Arizona Corporation Commission, have hereunto, set my hand and caused the official seal of this Commission to be affixed at the Capitol, in the City of Phoenix, this \_\_\_\_\_ day of \_\_\_\_\_, 2005.

\_\_\_\_\_  
BRIAN C. McNEIL  
Executive Director

DISSENT: \_\_\_\_\_

DISSENT: \_\_\_\_\_

EGJ:BGG:lhmvJG



SERVICE LIST FOR: UNS Gas, Inc.  
DOCKET NO. G-04204A-05-0046

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